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# Hormel Foods Corporation F2Q09 (Qtr End 04/26/09) Earnings Call Transcript

May 21, 2009 2:09 PM ET | **Hormel Foods Corporation (HRL)**

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## Q2: 2009-05-21 Earnings Summary

EPS of \$0.15 beats by \$0.02 | Revenue of \$1.60B (0.06% Y/Y) misses by \$77.42M

Hormel Foods Corporation (NYSE:HRL) Q2 2009 Earnings Call May 21, 2008 9:30 AM ET

### Executives

Kevin Jones – Director IR

Jeffrey Ettinger – President & CEO

Jody Feragen – SVP & CFO

### Analysts

Akshay Jagdale – Keybank

Farha Aslam - Stephens Inc.

Christina McGlone - Deutsche Bank

Jonathan Feeney - Janney Montgomery Scott

Chris Bledsoe - Barclays Capital

Ann Gurkin - Davenport & Company

## **Operator**

Welcome to the Hormel Foods second quarter earnings conference call. (Operator Instructions) I would now like to turn the conference over to Kevin Jones.

## **Kevin Jones**

Good morning. Welcome to the Hormel Foods conference call for the second quarter of fiscal 2009. We released our results this morning before the market opened around 6:30 am Central time. If you did not receive a copy of the release, you can find it on our website at [www.hormelfoods.com](http://www.hormelfoods.com) under the Investor section.

On our call today is Jeffrey Ettinger, Chairman of the Board, President and Chief Executive Officer and Jody Feragen, Senior Vice President and Chief Financial Officer. Jeffrey will provide a review of the operating results for the quarter and an outlook for the remainder of the fiscal year, then Jody will provide detailed financial results for the quarter. The line will be opened for questions following Jody's remarks.

An audio replay of this call will be available beginning at 10:30 am Central time today, May 21, 2009. The dial in number is 800-406-7325 and the access code is 4063374. It will also be posted on our website and archived for one year.

Before we get started with the results of the quarter, I need to reference the Safe Harbor statement. Some of the comments made today will be forward-looking and are made under the Private Securities Litigation Reform Act of 1995. Actual results may differ materially from those expressed in or implied by the statements we will be making.

Among the factors that may affect the operating results of the company are fluctuations in the cost and availability of raw materials and market conditions for finished products. Please refer to Pages 25 through 30 in the company's 10-Q for the quarter ended January 25, 2009 for more details. It can be accessed on our website.

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Now I'll turn the call over to Jeffrey.

**Jeffrey Ettinger**

Good morning, we were pleased with our results in the second quarter especially given the negative cut out margins in our pork operations, and the low commodity turkey meat prices. Our Q2 earnings of \$0.59 per share represent a 5% increase over our record results of a year ago.

While total sales were essentially flat at \$1.6 billion due to reduced basic processing tonnage in both our turkey and pork operations, sales of our branded meat products and grocery products groups were both up.

I will now take you through each segment. Our grocery product segment reported a dollar sales increase of 4% and a segment profit increase of 5% for the second quarter. Given the strong quarter we had in grocery products a year ago, this is an impressive result.

Double-digit increases in the sales of our SPAM family of products, Dinty Moore Stew and Hormel Chili were key drivers for grocery products. Sales of CHI-CHI'S in our Mexican products were also strong during the quarter.

Sales of our COMPLEATS microwave meals improved from last quarter thanks to increased promotional efforts. Sales comparisons for grocery products in the second quarter and in ensuing quarters will be affected by the dissolution of our joint venture for Capapelli Olive Oil. The new owners of the brand also distribute olive oil in the United States under the Bertoli and Carbonel brands and have chosen to consolidate these offerings outside of our venture.

We did generate a gain at the corporate level by virtue of the sale of our joint venture rights.

Our refrigerated food segment reported flat dollar sales and operating profit was down 7% from a year ago. The primary driver of this weaker performance was the negative cut out margin experienced throughout much of the quarter.

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Our Farmer John's subsidiary was pressured by these same difficult circumstances and also experienced negative margins in their farm operations. On the positive side our meat products group had an outstanding quarter achieving high single-digit sales growth in its branded portfolio of products.

We achieved double-digit sales growth in pepperoni, Natural Choice luncheon meats and Di Lusso deli company products. We also saw a turnaround from last quarter on sales of Hormel refrigerated entrées, Lloyds B-B-Q tub meats, and Hormel flavored marinated pork loins.

Food service sales within refrigerated foods continued to decline as the trend of eating more meals at home and decreased travel took their toll. Our Jennie-O Turkey Stores segment reported a sales decrease of 1% but an operating profit increase of 42%.

Lower feed expenditures due to our planned cuts in turkey production and a decrease in cost per ton was the primary driver of this improved profitability. Production was actually down low double-digits but sales volume only dropped 4% as we made a significant reduction in inventory.

This tightening of production allowed us to avoid generating surplus breast meat which would have been sold at a loss under current market conditions. The [inaudible] Jennie-O was also focused on moving more turkey into value added products during the quarter. A continuing success story was the Jennie-O Turkey Stores fresh tray pack turkey line of products.

The specialty foods segment reported decreased sales of 5%, down 8% excluding acquisitions, and operating profit was down 1%. Within the segment our specialty products group generated increased sales of private label canned meat products and our Diamond Crystal brand subsidiary achieved increased sales of the sugar substitutes and liquid portion products.

These successes were unable to completely offset weaker sales of nutritional and ready-to-drink products by our Century Foods subsidiary.

Our all other segment consisting primarily of our Hormel Foods international business reported increased dollar sales of 3% but a 14% decrease in operating profit. Export sales of fresh pork and the SPAM family of products strengthened, but were more then offset on the bottom line by a strong US dollar and weaker results by our joint ventures.

Overall our second quarter results once again demonstrate the benefits of our balance business model. I am proud that our team was able to do better then expected this quarter amidst the difficult operating environment.

Looking forward we still face a number of challenges to our business as a result of the unsettled economy. These include the continuing unfavorable cut out margins, the prevailing over supply of turkey commodity meats, uncertainty regarding commodity grain prices, continued weakness in the food service sector, and potential export issues.

Nonetheless we have a number of strengths that should allow us to deliver positive comps for the remainder of the year. These include solid sales momentum of our strong portfolio of branded products, the improvements we have made in matching our pricing to our costs, and our rock solid balance sheet which allows us to take advantage of strategic opportunities that present themselves.

Based on our positive results this quarter we now anticipate full year results in the upper end of our previously announced guidance range of \$2.15 to \$2.25 per share. At this time I will turn the call over to Jody Feragen, to discuss the financial information relating to the second quarter of fiscal 2009.

### **Jody Feragen**

Thank you Jeffrey, good morning everyone. Earnings for the fiscal 2009 second quarter totaled \$80.4 million, or \$0.59 per share compared to \$77.6 million or \$0.56 per share a year ago. Earnings for the first half of fiscal 2009 totaled \$161.8 million, compared to \$165.7 million a year ago.

Dollar sales for the second quarter totaled \$1.6 billion which is even with last year. For the first half of 2009 dollar sales increased 2% to \$3.3 billion. Volume for the second quarter was 1.1 billion pounds, down 2% from fiscal 2008.

Acquisitions added 6.3 million pounds to the quarter. Year to date, volume was 2.3 billion pounds, down 2% from fiscal 2008. Acquisitions added 11.8 million pounds to the first half of the year.

As Jeffrey indicated our turkey production was down double-digit due to the impact of reduced numbers and lower weights off the farm. Selling, general and administrative expenses in the second quarter were 8.8% of sales this year, even with last year.

Year to date the expenses were 8.6% of sales compared to 8.8% last year. We expect selling, general and administrative expenses to be approximately 9% of sales for the remainder of the year.

Advertising expenses were 1.6% of sales for the quarter, compared to 1.7% in 2008. Year to date, advertising expenses are 1.5% of sales compared to 1.7% in fiscal 2008. We have experienced lower media rates which improve our reach in frequency measures.

We expect advertising expenditures for fiscal 2009 to be approximately equal to our 2008 expense. Interest and investment income was \$8.6 million for the second quarter compared to income of \$3.3 million in fiscal 2008. For the current quarter we had higher returns on the rabbi trust investments versus last year, and as Jeffrey mentioned a \$3.6 million gain on the dissolution of the Carapelli joint venture.

Interest expense for the quarter was \$6.9 million compared to \$6.4 million last year. Year to date interest expense is \$14.4 million compared to \$13.1 million last year. We expect interest expense to be approximately \$28 million to \$29 million for the full year.

Our effective tax rate in the second quarter was 35.5% versus 36.1% in fiscal 2008. The year to date effective tax rate is 35.1% compared to 36.4% last year. We expect the effective tax rate for fiscal 2009 to be about 36%.

The basic weighted average number of shares outstanding for the second quarter and first six months of the year was 134 million shares. The diluted weighted average number of shares outstanding was \$135 million for the second quarter and the first half of the year.

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We did not repurchase any shares of common stock during the second quarter. We have 1.9 million shares remaining to be purchased from the 10 million share authorization in place.

Depreciation and amortization for the quarter was \$31 million which is even with last year. For the first half of the year depreciation and amortization was \$62 million compared to \$64 million last year. We expect the full year depreciation and amortization to be approximately \$125 million to \$130 million.

Total long-term debt at the end of the quarter was \$350 million. We ended the quarter with \$100 million outstanding on our line of credit. Year to date cash flow from operations improved over 2008 as we emphasized initiatives to reduce our working capital.

We have deliberately built our cash balances in response to the uncertain credit market. Given the improvement in our working capital and with somewhat more certainty in the credit markets, I would expect that we will be repaying our line of credit before the year is over.

Capital expenditures for the quarter totaled \$20 million compared to \$36 million last year. For the first six months of the year capital expenditures totaled \$46 million compared with \$68 million last year. For 2009 we expect capital expenditures to be about \$100 million.

At this time I will turn the call over for the question and answer portion of the call.

**Question-and-Answer Session**

**Operator**

(Operator Instructions) Your first question comes from the line of Akshay Jagdale – Keybank

**Akshay Jagdale – Keybank**

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Congratulations on a really good quarter first off and just a couple of questions, first of all your guidance, you said you intend to be in the high end of your range. If we take the high end it implies about 21% EPS growth over the prior years, for EPS, and that was down about 18%. So in my view it still seems a little conservative which is okay, but I just wanted to talk about that relative to your divisions. You highlighted some risks and for me, when I look at your Jennie-O turkey division the main risks there are corn and soybean prices as well as what's happening on the pricing and I think we're seeing an inflection point on the pricing side for commodity meat given what's happening on the supply side. So I just want you to talk a little bit about the risks in each section and what makes you a little bit conservative about your guidance, and the same thing on refrigerated foods, if you could talk about the cut out as being, its been weak, yet you had very good performance this quarter. I guess the bottom line is you had all those risks in this quarter yet you seem to have outperformed not only in the market but your own expectations so given that I'm just trying to see if there's any incremental risks going forward for each of those divisions.

### **Jeffrey Ettinger**

At the divisional level a couple of quick comments, on pricing inflection point, we certainly see the industry supply and demand getting in balance but we're not seeing the move in pricing yet. Breast meat is still very low, cold storage stocks are still very high. We're starting to head into the summer season and so it certainly should start correcting itself.

But in the meantime the quarter has already started and so we're not there yet. In terms of the refrigerated outlook, entering into this year we never expected the negative cut outs situation that we've been experiencing and you're correct that we had an excellent quarter from the branded standpoint and recovering most of that.

Now the cut out issue is still with us for right now and you can add to that a little bit of uncertainty now with the export markets on the heels of the H1N1 issue and so it does make us concerned. If both of those things were to clear up and we got back to more normalized cut outs and the export issues went away then we probably would be being a little more optimistic.

In terms of the overall rationale for where we ended up on the guidance, and when all was said and done we had a good second quarter, certainly up year over year, but we're flat for the year at this stage of the game and we had two of our five operating segments reporting a gain in the quarter and only one of five in the first quarter.

Our expectation for the second half is that we expect both quarters to be up. We expect to gain in the vicinity of \$0.15 plus or minus for the half and we expect the majority of segments to start generating gains. We don't anticipate at this point it will probably be all of them, but we're certainly seeing, we think we'll see some improvement there.

And so ultimately it does to us get all about delivering rather than forecasting and we've given you what we think is our best assessment given what we're up against right now and the momentum we have.

### **Akshay Jagdale – Keybank**

One more follow-up, but in terms of your cash, I know you talked about the credit environment but from all we're hearing the credit environment seems to be easing and looking at the cash per share, \$2.30 a share right now, typically it's around \$1.00 so it's really a lot higher than it used to be. You also have quite a bit of room on your balance sheet. Can you just talk a little bit about how you plan to use that going forward. You didn't buy back any shares this quarter either but I understand the comment about credit tightening etc., but it certainly seems to be easing so if you could talk a little bit about cash flow usage for the latter half of the year.

### **Jody Feragen**

Certainly and obviously we have some outstanding balances on our line of credit and that would be a thing that we can use that excess cash with. Other than that our cash priorities have not changed. We look to continue to invest in our businesses. We are continuing with the completion of the production facility in Dubuque, Iowa.

Given all that though we have seen our operations when we were initially challenged with these uncertain credit markets we asked people to prioritize their capital expenditure spending and you'll see that we're down year to date. I expect that to pick up in the back half. So we'll continue to invest there.

We do have the opportunity to repurchase shares and that was somewhat slowed down as we moved into this uncertain economic times and as you said, we're seeing a little bit better response on the credit side so that gives us the opportunity for cash there.

And then we obviously we'll continue to meet our commitments on dividends.

### **Operator**

Your next question comes from the line of Farha Aslam - Stephens Inc.

### **Farha Aslam - Stephens Inc.**

I noticed on your commentary somewhat of a pick up in convenience items in the retail channels, could you comment some more on those trends and how that's going thus far into the fiscal third quarter and the fiscal fourth quarter, is there any potential that we might be seeing a bottoming here, an improvement in that area.

### **Jeffrey Ettinger**

I definitely would go with your last statement about a bottoming and improvement. We had seen significant declines of in the COMPLEATS franchise starting in the third quarter last year, double-digit declines for a couple of quarters, its gotten somewhat better in the first quarter and then, yes, we saw it moderate and we're back to kind of a fairly even, slight gain position on the shelf stable side of the franchise.

Similarly we had seen declines not over as many quarters but we had seen some declines on the refrigerated entrées, the Hormel entrées and the Lloyds and this quarter, the second quarter was better. We're certainly trying to do what we can to address any issues consumers might have with the value proposition on those items.

I think we've said in prior calls to us, when all is said and done, a COMPLEATS meal in the mid \$2.00 range is still an excellent value and so we're being more aggressive about communicating that. We're certainly working with our retailers to work on positioning and pricing of the items on a feature basis and so I am encouraged that those businesses should be able to now start growing again going forward.

### **Farha Aslam - Stephens Inc.**

Just switching over quickly to the pork area, you made a quick allusion there to the H1N1 virus, just a follow-up, any color on how that is settling out and particularly in some of the markets. I know you talked about there was some strong results in Mexico, but anything that's changed on that sequentially in Mexico or other markets particularly with respect to hogs and pork.

**Jeffrey Ettinger**

Well we're more of a domestic player than some of our competitors in terms of where our pork ends up. What we saw domestically was the first couple weeks after the scare hit, we did see some declines, close to 10% decline in fresh pork volume.

The pork producers and others have been aggressive about putting out ads and we've been supportive of those and so we've seen a restoration of the domestic business. We have some excellent features heading into Memorial Day here for example.

In terms of export markets, it's a little hit and miss right now. There are some that are closed, there are some that have some fairly significant restrictions. Mexico, their issues really related more to demand. Their economy came to a screeching halt there with all the things going on in that country and so that really disrupted any normal flow there.

But we think that will come back to more reasonable levels.

**Farha Aslam - Stephens Inc.**

One last thing on the hog, pork situation, we've seen hog prices come back a little bit, what are you expecting just on a comparables basis hog prices this year versus last year, I guess for the remainder of the year.

**Jody Feragen**

I got out of the hog forecasting business because I think there's better forecasts that you can obtain publically but I guess we still see a contraction in the overall supply of hogs for the year but not as much as we originally anticipated. And I would expect that prices will be somewhat less than last year but higher than what we've seen in the first half of the year.

**Operator**

Your next question comes from the line of Christina McGlone - Deutsche Bank

**Christina McGlone - Deutsche Bank**

I wanted to understand, when you were talking about Jennie-O, you talked about drawing down inventory and that allowed you not to put surplus breast meat on the market, can you explain that. And what does that mean going forward if your inventory is now drawn down and when you're producing are we going to see more breast meat hit the market or you're using more of that meat internally now.

**Jeffrey Ettinger**

I didn't do a very good job of explaining that. First of all let's just talk production, we announced that production cut last year and that production cut is flowing through the system. We had announced 7% to 8%, and then we added a little bit to the cut and so when all is said and done we ended up in the low double-digit range of actual meat being produced in the plants during the quarter.

What I meant by inventory drawdown is we were similar to many others in the industry and this turkey stopped moving on an aggressive basis last fall and so we ended up with extra whole birds, we ended up with extra meat and we've been systematically kind of liquidating those positions so we don't sit on inventory.

We're now in a better position in terms of balance but the production cuts going forward will still be in place. So all I was trying to point out there was that our sales tonnage decline didn't match our production decline because we were still selling off that old inventory.

**Christina McGlone - Deutsche Bank**

So just not selling surplus breast meat is more of a production, it wasn't an inventory issue, just a drop in production.

**Jeffrey Ettinger**

Right and then strategically, that is what we're trying to do here is we're trying to tighten the system back down so that the meat we bring in is supportive of our value added portfolio and that we as much as possible stay out of the commodity meat games.

**Christina McGlone - Deutsche Bank**

Okay and then you had said this, but things that we observe like inventories and breast meat prices, still look weak, but you're outperforming and I'm curious if you still view 9% as normalized margins even though you're reducing your commodity exposure. So I assume it will fluctuate less than it has in the past and then could we get to above 9% this year given the dramatic production cuts in the industry and as demand seasonally picks up.

**Jeffrey Ettinger**

We are certainly making that effort to reduce the fluctuations in our overall performance to carve off the ends if we can. In terms of particular percentage goals, last year for the year, let's talk years first of all, we were at 5.9%. We've now turned the corner, we're into the realm of positive comps but we did start with a negative first quarter so our estimate for the year this year is probably more in the 7% to 8% range.

You'll see a better quarter than that in the fourth quarter but the business is a little bit seasonal in terms of when profit is delivered. Our longer-term goal for Jennie-O remains to work it up into that 8% to 10% range but you will not see that on an annualized basis in 2009.

**Christina McGlone - Deutsche Bank**

My last question, can you give an outlook for pork processing margins and then also when [Europe] meat products group did so well, is that, can you maybe talk about was it better promotional activity, lower input costs, better execution, just to give us an idea of what drove those strong results. And if that's expected to continue.

**Jeffrey Ettinger**

Well the processing margin picture is very cloudy. We're in situations that we have not normally encountered in terms of these multiple months of negative cut [evens] and so we're working through it but we don't have a very clean outlook for that.

In terms of meat products, you've got two things going on. Clearly on an internal basis as raw materials ended up lower than had originally been expected that benefits a profit contribution of those value added items. But what I'm really [pouting] when I'm talking about the strength of the meat products portfolio is the vibrancy of the demand for the products.

And we had a number of items that are up high single-digit, double-digit; pepperoni, Natural Choice, party trays, Di Lusso Deli Company, Black Label bacon, the recovery of the entrées and so that to me is attributable to new product innovation, to good marketing efforts, to good ad campaigns and to good work by our sales force to get the right pricing and feature of those items.

And that should continue.

### **Operator**

Your next question comes from the line of Jonathan Feeney - Janney Montgomery Scott

### **Jonathan Feeney - Janney Montgomery Scott**

I want to talk a little bit about the acquisition environment, I know you've been staying focused on the value added businesses but even those sorts of businesses it seems like you should be becoming more available as time goes on. Is there, what do you think about the acquisition environment right now and has it improved or stayed the same, or gotten less attractive over the past quarter.

### **Jeffrey Ettinger**

Well it's a mixed bag. There's probably more distress oriented properties available but we've never really been a distress player. We're not a turnaround oriented acquirer. We're much more interested in fit and then growth opportunities. I could also make a case right now that to the extent maybe half the acquisitions we've bought over the last few years had some kind of family ownership connection.

And again absent the stress, this is not particularly a good market for families to be considering selling their life work to another company and so we're probably seeing maybe even less interest there. Now on the positive side there is, value is certainly better in this environment and competition arguably would be less within some of the protein spaces.

Some of the other entities that have been very aggressive in the past are now talking about focusing on restoration of their balance sheets and so that could provide opportunities also.

**Jonathan Feeney - Janney Montgomery Scott**

How about your focus, has your focus changed as far as what you think a fit could be based on the opportunity set that's out there.

**Jeffrey Ettinger**

No, we're still looking at most likely it would be in areas that we're already in that we bring something to the party beyond just our money. We like food service, we like deli, we like canned items and value added branded protein items. On an export basis we've said very clearly our focus is in Asia and that we would like to increase our footprint in that market and we would be interested in something there as well.

**Jonathan Feeney - Janney Montgomery Scott**

That's a good [seg] actually because my other question was going to be about food service, historically one of the strengths of Hormel has been an over exposure and I think excellent execution against the food service opportunity within meats, have you seen, you're seeing better performance in refrigerated foods, are you seeing any kind of substantial pick up in food service interest, in food service pipeline, and I guess what's your outlook for that business for the remainder.

**Jeffrey Ettinger**

It's still pretty soft, food service. We're not used to reporting declining sales numbers in that segment but that's the reality they're facing. They're doing a nice job of promoting innovative items and of attacking the parts of the segment that are still somewhat more healthy, the non commercial side for example.

And we have areas where the picture is a little better, the Diamond Crystal unit for example had a very nice quarter. They sell more to the QSR trade and that's not down as much as some of the other parts of food service. But we're not seeing, its not in a freefall. In some areas it seems to have stabilized but we're not seeing any immediate sign of pick up.

**Operator**

Your next question comes from the line of Chris Bledsoe - Barclays Capital

**Chris Bledsoe - Barclays Capital**

I just wanted to clarify briefly, your fresh pork spreads today, are they better or worse then where we were pre H1N1 level.

**Jody Feragen**

Today we're still seeing those upside down as I call them so the Western Corn Belt price is higher then the cut out.

**Jeffrey Ettinger**

The outbreak seemed to stem what we had hoped would be some momentum toward restoration of a normal market but to say better or worse given that a number of these months haven't been very good, kind of pick a date, its better then some and worse then others.

**Chris Bledsoe - Barclays Capital**

They're still down but not necessarily seeing the seasonal lift that you might otherwise sometimes see or—

**Jeffrey Ettinger**

I think it pulled the rug out from under the trend that would have happened seasonally but that doesn't mean its not still going to get back into balance.

**Jody Feragen**

We certainly anticipated on our call in the first quarter that it was a short-term phenomenon but it seems to have lasted quite a bit longer than we anticipated.

**Chris Bledsoe - Barclays Capital**

And then I guess with that, I'm sort of, I'm wondering if you're worried about the health of your hog suppliers and I guess the intermediate term production capacity comes out of the system and also whether you're hearing from lenders anything to suggest that they're growing less patient on a hog cycle recovery that's now 18 months well into a trough cycle anyway.

**Jeffrey Ettinger**

This was certainly a tough development on the supply side and it was a tough development to the extent we have live production assets for parts of our business. This is the time of year usually there's, you would see the recovery and they would be able to get in a better position.

Although it's something that we have to monitor closely, we have to talk with them a lot. We take some comfort in the fact that the up cycle lasted three to four years and so hopefully the stronger ones at least are in a reasonable position against that, but clearly moving forward at some point something would have to give.

**Chris Bledsoe - Barclays Capital**

And just looking at the broader equity market picture right now, it seems to be, I'd argue anticipating a kind of V shaped recovery, it seemed a little premature to me but if consumer purchase behavior continues to follow suit and it sounds like you're seeing a little bit of that, I'm wondering if the risk of pantry de loading on some of your canned items could be or would be fully offset by improved sales of convenience items.

**Jeffrey Ettinger**

There certainly could and probably will come a point where comp sales on canned items aren't going to be double-digit. That wasn't the trend we were on before. We do believe we've augmented those sales by introducing some nice extension innovation such as SPAM singles and Dinty Moore big bowls and Hormel Chili Master and those are contributing to the growth.

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And those are quite early in their life spans. But we did see very solid growth from a number of items, value is in the eye of the consumer. Party trays are over \$10.00 a piece and so they're certainly not a low priced item yet those sales continue to register at double-digit gain clips because I think consumers do deem them a good value for what they're used for.

And so I think our portfolio is strong enough overall that even if we did see some mitigation of the growth on the canned items, we would make up for it in convenience and we would at that point probably start seeing some food service buoyancy.

### **Chris Bledsoe - Barclays Capital**

And just to follow-up on acquisitions and you've been to your credit, very patient over the last couple of years, or the last 18 months anyway, and I'm now trying to get a sense with seeing the prospect for continued improvement and market sentiment and the implication that may have for asset valuation, I'm trying to get a sense of whether or not your urgency or sense of urgency has changed in any way in the last couple of months around pulling a trigger on potential acquisitions.

### **Jeffrey Ettinger**

No I wouldn't say its changed. We've been interested all along. We recognize that we've been in certainly a slower period of delivering a deal that we can talk about to the street versus say the time period in early 2005 when we had four of them happen in three months.

But there's an ebb and flow to deals and your analysis of them. There was probably a moment there in the fall where when the credit markets were so ridiculous that had we had something on the verge of happening we might have been nervous about getting financing for it and that could have impacted our views.

But otherwise our mindset is we'd love to find things that are a good fit and that we could acquire at a reasonable value.

### **Operator**

Your next question comes from the line of Ann Gurkin - Davenport & Company

### **Ann Gurkin - Davenport & Company**

Just wanted to follow along a little bit on the discussion about the security of supply of hogs, its our understanding that one of your suppliers could decide to sell assets, so would you take or look at the opportunity to maybe add to assets in the hog production area to secure supply.

**Jeffrey Ettinger**

Well I'm assuming we're not talking about any particular supplier. I'm not sure who you're referencing and I wouldn't be able to talk about it anyway. I can talk about philosophically, we're not overly keen on adding volatility to our business through more exposure to live production assets at this point. We don't mind the participation level we have.

Its certainly, we think we've brought in some knowledge and skill to the segment by being involved in it but we also recognize that ultimately we certainly profess to be and think we are primarily a packaged food company and so the more of those types of downstream assets that we get involved with, the further away from that consistent story we move.

So our goal would be to continue to maintain supplies through the kind of family farm, contract connections that we have for most of our business.

**Ann Gurkin - Davenport & Company**

And then I'd be interested in your comments on the supply of hogs in China, do you think, we're hearing stories that China maybe is in an over supply situation of hogs and I'd just be curious, I'd like your insight on that.

**Jeffrey Ettinger**

Well we've heard a short-term assessment of that, that our sense is that perhaps in that country there's been a stronger reaction to H1N1 fear then there has been in this country and in the short run that has potentially backed up pork supplies but its pretty early in the game to assess whether that's going to continue or whether that should, and our hope is that that will go away here soon.

**Ann Gurkin - Davenport & Company**

And then on grain, I don't know if you care to look into your crystal ball and give us your thoughts on the outlook for corn and soybean prices, certainly we're facing a delayed planting in the East Coast for corn, and in a smaller crop of soybeans out of South America. I don't know if you'd care to comment at all.

**Jeffrey Ettinger**

Well those are important factors. We certainly are rooting for the right weather to make sure that the farmers in those regions can engender a reasonable crop. Our year and our pricing is sort of built on an assessment that corn will be in the, anywhere from \$3.50 to \$5.00. Its kind of been in that vicinity since the big run up last summer. It pretty much lived in that range and so our best assessment right now is we'll continue to live in that range.

But clearly a really disastrous event from a weather standpoint could impact that. Our sense now is hopefully that's not going to happen.

**Operator**

Your next question is a follow-up from the line of Akshay Jagdale – Keybank

**Akshay Jagdale – Keybank**

Just focusing a little bit on grocery products, can you talk a little bit about the chili category and the exit of one of your key competitors and just maybe talk a little bit about longer-term trends in that division and where you could see normalized margin. That division obviously had close to 20% EBIT margins at one point, so if you could comment on that.

**Jeffrey Ettinger**

Well the division, without getting into a lot of detail on it, I will concede that the divisional results over a stretch of years clearly were impacted by what we call the chili wars or the major entrance by both Campbell's and Bush into the marketplace three, four years ago caused a lot of new advertising money to go into the category including by us, caused a lot of new promotional money to go into the category including by us.

And so as those entrances made their decisions about what to do with their franchises and as our team has redoubled its effort to retain our share and to make sure that we're still the leader in that category we're certainly in a better, more normalized position with that category.

We continue in addition to them leaving, we're really focused on again driving innovation and we've done it through simple things like adding easy [open] tops to our basic canned products and then more elaborate innovations such as the microwavable trays, the microwavable bowls, and the premium glass jar Chili Master item.

And our intention, we think chili is a great category to be in, we're the clear leader and we expect to continue to drive growth in that area.

### **Akshay Jagdale – Keybank**

I think one thing that everyone seems to misunderstand quite a bit and this quarter is a perfect example and maybe you could clarify a bit is your refrigerated foods business, you have three parts in there the way I see it, meat products, food service, and then the pork business, the fresh and everything else and it seems like if I just look at year over year change in spreads for the market, fresh cut out versus the year over year change in your spreads, you have about only a third of the variability that the market show. And we've quantified that only a third of your portfolio within refrigerated foods moves really with the market and is impacted by the commodity prices and that sort of came through this quarter. So there's been, everyone keeps asking about hog prices and the weak cut out etc., but like you said and you highlighted your meat products division was up high single-digits and it just seems like its very misunderstood, so maybe you could just talk about the portion of your business that's commoditized.

### **Jeffrey Ettinger**

I can't verify the quantification you provided but I think in general your thoughts make sense that overall of the refrigerated foods sales, a billion dollars of the sales are in the branded meat product area and a billion dollars of the sales are in the food service area where we've focused on value added branded products and so clearly we expect to kind of drive those results on a consistent basis and react on a pricing basis to what's going on underneath it in the marketplace.

And then even within the pork complex, we've made quite an effort over the years to brand as much of that as possible as well. We have our Always Tender franchise, we have our joint venture with Precept and other fresh port programs.

And so I do think overall we've done a lot of things in that division to make it a consumer oriented, consumer products type division and to be able to mitigate those big swings through the branded products.

### **Operator**

Your final question is a follow-up from the line of Chris Bledsoe - Barclays Capital

### **Chris Bledsoe - Barclays Capital**

Just looking at the back half guidance, and on my numbers it actually implies a sequential deterioration in operating margin, and looking back I don't see really any reason seasonally why back half would necessarily be above or below the second quarter operating margin. So I'm trying to get a sense of whether your guidance implies this deterioration entirely because of known variables that you've discussed currently impacting your business or whether you're just kind of leaving some flexibility to deal with either unknown variables as headwinds or maybe worse than expected magnitude of the impacts from the known headwinds.

### **Jeffrey Ettinger**

Well as I indicated earlier we do expect the majority of our business operating segments to be up. We otherwise, and I do think what we've tried to factor in as best we can what our anticipation is of the challenges in the export area and the cut out area and then we've made as good a guess as we think we can in terms of the impact on some of the below the line factors that hit last year and what might happen this year.

So I guess that's as good a characterization as I can give. We tried to kind of go all in with that and give you our best shot. At this point its what we think it adds up to.

### **Chris Bledsoe - Barclays Capital**

So your guidance I guess this is kind of the question, your guidance is a best shot, not necessarily a best shot but, hey guys why don't we just leave ourselves a little bit of flexibility here should things deteriorate beyond what the current picture even suggests.

**Jeffrey Ettinger**

I guess I don't know how to answer that question without casting aspersions on the guidance, so I'm just going to have to leave it I guess.

**Operator**

There are no additional questions at this time; I would like to turn it back over to management for any additional or closing comments.

**Kevin Jones**

Thank you all for joining us today.

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